

CHARITON MUNICIPAL WATERWORKS
CHARITON, IOWA

INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS

JUNE 30, 2006

Peak & Gerdes, LLP
Certified Public Accountants
1051 Office Park Road
West Des Moines, IA 50265

Table of Contents

	<u>Page</u>
Officials	3
Independent Auditor's Report	5-6
Management's Discussion and Analysis	7-10
Basic Financial Statements:	<u>Exhibit</u>
Proprietary Fund Financial Statements:	
Statement of Net Assets	A 12
Statement of Revenues, Expenses and Changes in Fund Net Assets	B 13
Statement of Cash Flows	C 14-15
Notes to Financial Statements	16-21
Required Supplementary Information:	
Budgetary Comparison Schedule of Receipts, Disbursements and Changes in Balances - Budget and Actual (Cash Basis)	23
Budget to GAAP Reconciliation	24
Notes to Required Supplementary Information - Budgetary Reporting	25
Other Supplementary Information:	<u>Schedule</u>
Schedule of Operating Expenses	1 27
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <u>Government Auditing Standards</u>	28-29
Schedule of Findings	30-33

CHARITON MUNICIPAL WATERWORKS

OFFICIALS

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
George Holder	Chairman	December 31, 2009
Roger Bingham	Vice-Chairman	December 31, 2011
Byron Welch	Secretary	December 31, 2007
James F. Corbett	Superintendent	Indefinite
Ruth A. Ryun	Treasurer	Indefinite

Chariton Municipal Waterworks

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Independent Auditor's Report

To the Board of Trustees
Chariton Municipal Waterworks

We have audited the accompanying financial statements of the business type activities of the Chariton Municipal Waterworks, Chariton, Iowa, as of and for the year ended June 30, 2006, which collectively comprise the Waterworks' basic financial statements listed in the table of contents. These financial statements are the responsibility of the Waterworks' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements of the Chariton Municipal Waterworks are intended to present only the results of the transactions of that portion of the financial reporting entity of the City of Chariton that is attributable to the transactions of the Waterworks.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business type activities of the Chariton Municipal Waterworks, at June 30, 2006, and the respective changes in financial position and cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated September 26, 2006, on our consideration of the Chariton Municipal Waterworks internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 7 through 10 and 23 through 25 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Chariton Municipal Waterworks' basic financial statements. Other supplementary information included in Schedule 1, is presented for the purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Peak & Gerdes, LLP
Certified Public Accountants

September 26, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

Chariton Municipal Waterworks (Waterworks) provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2006. We encourage readers to consider this information in conjunction with the Waterworks financial statements, which follow.

The Waterworks is a component unit of the City of Chariton, Iowa.

2006 FINANCIAL HIGHLIGHTS

- Revenues of the Waterworks business type activities increased 14%, or approximately \$141,000, from fiscal 2005 to fiscal 2006.
- Expenses decreased 1%, or approximately \$10,000, in fiscal 2006 from fiscal 2005.
- The Waterworks net assets increased 3%, or approximately \$105,000, from June 30, 2005 to June 30, 2006.

USING THIS ANNUAL REPORT

The annual report consists of a series of financial statements and other information, as follows:

Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the Waterworks financial activities.

Proprietary Fund Financial Statements consist of a Statement of Net Assets and a Statement of Revenues, Expenses and Changes in Fund Net Assets and a Statement of Cash Flows. These provide information about the activities of the Waterworks as a whole and present an overall view of the Waterworks finances.

The Financial Statements tell how governmental services were financed in the short term as well as what remains for future spending.

Notes to Financial Statements provide additional information essential to a full understanding of the data provided in the basic financial statements.

Required Supplementary Information further explains and supports the financial statements with a comparison of the Waterworks budget for the year.

Other Supplementary Information provides detailed information about the Waterworks Funds.

REPORTING THE WATERWORKS FINANCIAL ACTIVITIES

Proprietary Fund Financial Statements

One of the most important questions asked about the Waterworks finances is, "Is the Waterworks as a whole better or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Fund Net Assets report information which helps answer this question. These statements include all assets and liabilities using the accrual basis of accounting and the economic resources measurement focus, which is similar to the accounting used by most private sector companies. All of the current year's revenues and expenses are taken into account, regardless of when cash is received or paid.

The Statement of Net Assets presents all of the Waterworks assets and liabilities, with the difference between the two reported as "net assets". Over time, increases or decreases in the City's net assets may serve as a useful indicator of whether the financial position of the Waterworks is improving or deteriorating.

The Statement of Activities presents information showing how the Waterworks net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods.

The Statement of Net Assets and the Statement of Activities report the following kind of activity:

- Business type activities include the Waterworks. These activities are financed primarily by user charges.

Fund Financial Statements

Proprietary funds account for the Waterworks Enterprise Funds. These funds report services for which the Waterworks charges customers for the service it provides. The Waterworks is responsible for ensuring the assets reported in these funds are used only for their intended purposes and by those to whom the assets belong.

The financial statements required for proprietary funds include a statement of net assets, a statement of revenues, expenses and changes in fund net assets and a statement of cash flows.

FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of financial position. The analysis that follows focuses on the changes in the net assets for business type activities.

Net Assets (Expressed in Thousands)		
	June 30,	
	2006	2005
Current and other assets	\$ 913	1,017
Capital assets	3,726	3,628
Total assets	4,639	4,645
Long-term debt outstanding	1,011	1,142
Other liabilities	51	31
Total liabilities	1,062	1,173
Net assets:		
Invested in capital assets, net of related debt	2,821	2,583
Restricted	410	503
Unrestricted	346	386
Total net assets	\$ 3,577	3,472

Net assets of business type activities increased from FY05 by approximately \$105,000, or 3.0%. The largest portion of the Waterworks net assets is the invested in capital assets (e.g., land, infrastructure, buildings and equipment), less the related debt. The debt related to the investment in capital assets is liquidated with sources other than capital assets. Restricted net assets represent resources that are subject to external restrictions, constitutional provisions or enabling legislation on how they can be used. Unrestricted net assets, the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants, legislation or other legal requirements, is approximately \$346,000 at the end of this year.

	Changes in Net Assets (Expressed in Thousands)	
	Year ended June 30,	
	2006	2005
Revenues:		
Program revenues:		
Charges for service	\$ 1,111	982
General revenues:		
Unrestricted investment earnings	29	10
Miscellaneous	32	40
Total revenues	1,172	1,032
Program expenses:		
Water	1,067	1,078
Total expenses	1,067	1,078
Increase (Decrease) in net assets	105	(46)
Net assets beginning of year	3,472	3,518
Net assets end of year	\$ 3,577	3,472

INDIVIDUAL MAJOR FUND ANALYSIS

Proprietary Fund Highlights

The Water Fund, which accounts for the operation and maintenance of the Waterworks, ended fiscal 2006 with a \$3,577,328 net asset balance compared to the prior year ending net asset balance of \$3,472,060.

BUDGETARY HIGHLIGHTS

The Chariton Municipal Waterworks prepares a budget on the cash basis of accounting and submits it to the City of Chariton. Over the course of the year, the Waterworks amended its budget one time, increasing budgeted disbursements by \$75,000. The Waterworks receipts were less than the budgeted receipts. However, budgeted disbursements were \$141,241 less than actual disbursements.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2006, the Waterworks had approximately \$3.7 million invested in a broad range of capital assets, including land, buildings, equipment, vehicles and infrastructure. This is a net increase (including additions and deletions) of approximately \$97,000, or 2.7 percent over last year.

Capital Assets at Year End (Expressed in Thousands)		
	June 30,	
	2006	2005
Land	\$ 48	48
Construction in progress	339	-
Improvements and buildings	69	94
Equipment and vehicles	51	68
Infrastructure	3,219	3,418
Total	\$ 3,726	3,628

The Waterworks had depreciation expense of \$254,531 in FY06 and total accumulated depreciation of \$5,350,369 at June 30, 2006. More detailed information about the Waterworks capital assets is presented in Note 4 to the financial statements.

For business type activities, major additions included purchase of a pickup, water tower repair and water main replacements.

Long-Term Debt

At June 30, 2006, the Waterworks had approximately \$1,011,000 in revenue notes and other debt outstanding compared to approximately \$1,142,000 at June 30, 2005, as shown below.

Outstanding Debt at Year End (Expressed in Thousands)		
	June 30,	
	2006	2005
Revenue notes	\$ 905	1,045
Compensated absences	106	97
Total	\$ 1,011	1,142

Additional information about the Waterworks long-term debt is presented in note 5 to the financial statements.

ECONOMIC FACTORS BEARING ON THE WATERWORKS FUTURE

Several economic factors affected decisions made by the Waterworks in setting its fiscal 2007 budget, including building a new ground storage tank, repair of claricones and aerator at the treatment plant, extension of 10" transmission mains to the north end of town, addition of a new 6" main in NW Chariton, and modifications to clearwell at plant to comply with federal regulations.

In fiscal year 2007, the Waterworks had approximately \$500,000 in uncompleted construction projects. These contracts are for water tower repair, water main replacement and water plant improvements. These projects will be paid for with a State Revolving Fund loan from the Iowa Department of Natural Resources.

CONTACTING THE WATERWORKS FINANCIAL MANAGEMENT

This financial report is designed to present our citizens, taxpayers, customers, investors and creditors with a general overview of the Waterworks finances to show the Waterworks accountability for the money it receives. If you have any questions or require additional information please contact the Waterworks Superintendent, 101 Albia Road, Box 861, Chariton, Iowa 50049.

Basic Financial Statements

CHARITON MUNICIPAL WATERWORKS

Exhibit A

STATEMENT OF NET ASSETS

June 30, 2006

	<u>Business Type Activities</u>
Assets	
Cash and pooled investments	\$ 289,477
Receivables, net of allowance for uncollectible amounts (\$11,637)	
Accounts, consumers and other	147,015
Estimated unbilled usage	24,524
Accrued interest	705
Inventories	8,201
Prepaid Insurance	17,255
 Restricted assets	
Cash and pooled investments	410,555
 Cost of bond issue (net of accumulated amortization)	15,828
 Capital assets (net of accumulated depreciation)	<u>3,725,649</u>
Total assets	<u>4,639,209</u>
 Liabilities	
Accounts payable	47,173
Accrued interest payable	3,653
Long - term liabilities:	
Portion due or payable within one year:	
Revenue bonds payable	145,000
Compensated absences	106,055
Portion due or payable after one year:	
Revenue bonds payable	<u>760,000</u>
Total liabilities	<u>1,061,881</u>
 Net Assets	
Invested in capital assets, net of related debt	2,820,649
Restricted for:	
Meter deposits	85,957
Reserve	195,000
Revenue bond retirement	15,737
Funded replacement	113,861
Unrestricted	<u>346,124</u>
Total net assets	<u>\$ 3,577,328</u>

See notes to financial statements.

CHARITON MUNICIPAL WATERWORKS
STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS

Exhibit B

Year ended June 30, 2006

Operating revenues:	
Charges for service:	
Water	\$ 1,107,840
Customer service and sale of materials	3,503
Total operating revenues	<u>1,111,343</u>
Operating expenses:	
Business type activities:	
Plant operation	274,688
Distribution operation	192,043
Accounting and collection	164,372
Administration	112,663
Repairs and minor equipment	16,134
Depreciation and amortization	<u>257,369</u>
Total operating expenses	<u>1,017,269</u>
Operating income	<u>94,074</u>
Nonoperating revenues (expenses):	
Interest income	29,227
Interest expense	(50,248)
Miscellaneous	<u>32,215</u>
Total nonoperating revenues (expenses)	<u>11,194</u>
Change in net assets	105,268
Net assets, beginning of year	<u>3,472,060</u>
Net assets, end of year	<u>\$ 3,577,328</u>

See notes to financial statements.

CHARITON MUNICIPAL WATERWORKS

Exhibit C

STATEMENT OF CASH FLOWS

Year ended June 30, 2006

Cash flows from operating activities:	
Cash received from customers and users	\$ 1,101,517
Cash received from other revenues	3,503
Cash paid for personal services	(333,160)
Cash paid to suppliers	<u>(391,080)</u>
Net cash provided by operating activities	<u>380,780</u>
Cash flows from noncapital financing activities:	
Miscellaneous income	<u>32,215</u>
Cash flows from capital and related financing activities:	
Acquisition of capital assets	(351,719)
Principal paid on revenue bonds	(140,000)
Interest paid on revenue bonds	<u>(50,832)</u>
Net cash used for capital and related financing activities	<u>(542,551)</u>
Cash flows from investing activities:	
Interest on investments	<u>29,042</u>
Net (decrease) in cash and cash equivalents	(100,514)
Cash and cash equivalents at beginning of year	<u>800,546</u>
Cash and cash equivalents at end of year	<u>\$ 700,032</u>

See notes to financial statements.

CHARITON MUNICIPAL WATERWORKS

Exhibit C

STATEMENT OF CASH FLOWS

Year ended June 30, 2006

Reconciliation of operating income to net cash

provided by operating activities:

Operating income	\$	94,074
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization expense		257,369
(Increase) in receivables		(6,323)
Decrease in inventories		5,109
Decrease in prepaid insurance		1,509
Increase in accounts payable and compensated absences		29,042
Net cash provided by operating activities	\$	<u>380,780</u>

**Reconciliation of cash and cash equivalents at year end to
specific assets included on the Statement of Net Assets:**

Current assets:		
Cash and pooled investments	\$	289,477
Restricted assets:		
Cash and pooled investments:		
Meter deposits		85,957
Reserve		195,000
Revenue bond retirement		15,737
Funded replacement		113,861
Cash and cash equivalents at year end	\$	<u>700,032</u>

See notes to financial statements.

CHARITON MUNICIPAL WATERWORKS

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

Note 1. Summary of Significant Accounting Policies

The Chariton Municipal Waterworks is a component unit of the City of Chariton, Iowa, as determined by the criteria specified by the Governmental Accounting Standards Board. The Waterworks operates under a trustee form of government provided by the Code of Iowa. A three-member board of trustees is appointed by the City Council of Chariton to six year staggered terms. The Waterworks provides water service to residents, businesses and industry in Chariton.

The financial statements of the Chariton Municipal Waterworks have been prepared in conformity with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board.

A. Reporting Entity

For financial reporting purposes, Chariton Municipal Waterworks has included all funds, organizations, account groups, agencies, boards, commissions and authorities. The Waterworks also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Waterworks are such that exclusion would cause the Waterworks financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Waterworks to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Waterworks. These financial statements present the Chariton Municipal Waterworks and there are no component units to be presented. The Waterworks is legally separate, but financially accountable to the City of Chariton. The Chariton City Council appoints the board and the legal budget is subject to approval by the City Council.

B. Basis of Presentation

Proprietary Fund Financial Statements – The Statement of Net Assets report information on all of the nonfiduciary activities of the Waterworks. The business type activities rely to a significant extent on fees and charges for services.

The Statement of Net Assets presents the Waterworks nonfiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories.

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt attributable to the acquisition, construction or improvement of those assets.

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions, enabling legislation or through Board of Trustee action.

Unrestricted net assets consist of net assets not meeting the definition of the two preceding categories. Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified.

The accounts of the Waterworks are organized on the basis of funds. The operations are accounted for by providing a separate set of self-balancing accounts which comprise its assets, liabilities, net assets, revenues and expenses. The water accounts are classified in the Enterprise Fund. The Enterprise Fund is utilized to finance and account for the acquisition, operation and maintenance of governmental facilities and services that are supported by user charges.

Note 1. Summary of Significant Accounting Policies (continued)

C. Measurement Focus and Basis of Accounting

The proprietary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been satisfied.

The proprietary funds of the Waterworks apply all applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Waterworks Enterprise Funds is charges to customers for sales and services. Operating expenses for Enterprise Funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as non-operating revenues and expenses.

The Waterworks maintains its financial records on the cash basis. The financial statements of the Waterworks are prepared by making memorandum adjusting entries to the cash basis financial records.

D. Assets, Liabilities and Fund Equity

The following accounting policies are followed in preparing the financial statements:

Cash, Pooled Investments and Cash Equivalents – The cash balances of most Waterworks funds are pooled and invested. Investments consist of non-negotiable certificates of deposit which are stated at cost.

For the purposes of the statement of cash flows, all short-term cash investments that are highly liquid (including restricted assets) are considered to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash and, at the day of purchase, have a maturity date no longer than three months.

Customer Accounts and Unbilled Usage – Accounts receivable are recorded in the Enterprise Funds at the time the service is billed. Unbilled usage for service consumed between periodic scheduled billing dates is estimated and is recognized as revenue in the period in which the service is provided.

Inventories - Inventories are valued at cost using the first-in / first-out method. Inventories in the Enterprise Funds consist of materials and supplies. Inventories are recorded as expenses when consumed rather than when purchased.

Restricted Assets - Funds set aside for payment of Enterprise Fund revenue notes are classified as restricted assets since their use is restricted by applicable note indentures. Other restricted assets include meter deposits restricted for application to unpaid customer accounts or for refund to customers, a reserve fund and a funded replacement fund, as required by the revenue note indentures.

Note 1. Summary of Significant Accounting Policies (continued)

Capital Assets – Capital assets, which include property, equipment and vehicles and infrastructure assets (e.g. roads, bridges, curbs, gutters, sidewalks and similar items which are immovable and of value only to the government) are reported in the applicable business type activities columns in the Statement of Net Assets. Capital assets are recorded at historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. The costs of normal maintenance and repair not adding to the value of the asset or materially extending asset lives are not capitalized. Reportable capital assets are defined by the Waterworks as assets with initial, individual costs in excess of the following thresholds and estimated useful lives in excess of two years.

Asset Class	Amount
Land, buildings and improvements	\$1,000
Equipment and vehicles	1,000
Infrastructure	1,000

Capital assets of the Waterworks are depreciated using the straight line method over the following estimated useful lives:

Asset Class	Estimated Useful Lives (In Years)
Improvements other than buildings	10-50 years
Vehicles	5 years
Equipment	5-10 years
Infrastructure	20-40 years

Compensated Absences – Waterworks employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, death or retirement. A liability is recorded when incurred in the government-wide fund financial statements. The compensated absences liability has been computed based on rates of pay in effect at June 30, 2006.

Long-term Liabilities – In the financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable business type activities column in the Statement of Net Assets.

E. **Budgets and Budgetary Accounting**

The Waterworks adopts a cash basis budget for operating purposes. The Waterworks also submits a cash basis (legal) budget to the City Council for approval in the City's budget process. The legal budget may be amended during the year utilizing the statutory procedures available to the City.

The budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended June 30, 2006, disbursements exceeded the amounts budgeted in the business type activities function.

Note 2. Cash and Pooled Investments

The Waterworks deposits in banks at June 30, 2006 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Waterworks is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The Waterworks had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement No. 3, as amended by Statement No. 40.

Note 3. Bond Issue Costs

The costs relating to the issuing of the revenue bonds are being amortized over the term of the bonds.

Note 4. Capital Assets

Capital assets activity for the year ended June 30, 2006 was as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Business type activities:				
Capital assets not being depreciated:				
Land	\$ 47,900	-	-	47,900
Construction in progress	-	338,772	-	338,772
Total capital assets not being depreciated	47,900	338,772	-	386,672
Capital assets being depreciated:				
Improvements and buildings	324,452	-	-	324,452
Equipment and vehicles	351,550	12,947	-	364,497
Infrastructure, water network	8,000,397	-	-	8,000,397
Total capital assets being depreciated	8,676,399	12,947	-	8,689,346
Less accumulated depreciation for:				
Improvements and buildings	230,387	24,745	-	255,132
Equipment and vehicles	283,741	29,776	-	313,517
Infrastructure, water network	4,581,710	200,010	-	4,781,720
Total accumulated depreciation	5,095,838	254,531	-	5,350,369
Total capital assets being depreciated, net	3,580,561	(241,584)	-	3,338,977
Business type activities capital assets, net	\$ 3,628,461	97,188	-	3,725,649

Depreciation expense was charged to the business type activities – water fund.

Note 5. Changes in Long-Term Liabilities

A summary of changes in long-term liabilities for the year ended June 30, 2006 is as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year	Due Within one Year
Business type activities:					
Revenue bonds	\$1,045,000	-	140,000	905,000	145,000
Compensated absences	97,438	8,617	-	106,055	106,055
Total	<u>\$1,142,438</u>	<u>8,617</u>	<u>140,000</u>	<u>1,011,055</u>	<u>251,055</u>

Revenue Bonds Payable

Annual debt service requirements to maturity for revenue bonds which were issued to finance water system improvements are as follows:

Year Ending June 30,	1992 Issue			1998 Issue			Total	
	Interest Rates	Principal	Interest	Interest Rates	Principal	Interest	Principal	Interest
2007	6.40%	\$ 45,000	\$ 6,130	4.45%	\$ 100,000	\$ 37,707	\$ 145,000	\$ 43,837
2008	6.50%	50,000	3,250	4.50%	105,000	33,258	155,000	36,508
2009				4.60%	110,000	28,533	110,000	28,533
2010				4.65%	115,000	23,473	115,000	23,473
2011				4.70%	120,000	18,125	120,000	18,125
2012				4.75%	125,000	12,485	125,000	12,485
2013				4.85%	135,000	6,547	135,000	6,547
Total		<u>95,000</u>	<u>\$ 9,380</u>		<u>810,000</u>	<u>\$ 160,128</u>	<u>905,000</u>	<u>\$ 169,508</u>
Less current portion		<u>45,000</u>			<u>100,000</u>		<u>145,000</u>	
		<u>\$ 50,000</u>			<u>\$ 710,000</u>		<u>\$ 760,000</u>	

The resolution providing for the issuance of the 1992 revenue bonds include the following provisions:

- (A) The bonds will only be redeemed from the future earnings of the Waterworks and the bondholders hold a lien on the future earnings.
- (B) \$45,000 will be set aside in a "Reserve Fund".
- (C) A sum of 1/6 of the interest coming due on the next succeeding interest payment date plus 1/12 of the next succeeding principal payment date shall be paid into a "Sinking Fund".
- (D) \$850 per month will be deposited to an "Improvement and Extension Fund" until a sum of \$50,000 is accumulated.

The resolution providing for the issuance of the 1998 revenue bonds include the following provisions:

- (A) The bonds will only be redeemed from the future earnings of the Waterworks and the bondholders hold a lien on the future earnings.
- (B) \$140,000 will be set aside in a "Reserve Fund".
- (C) A sum of 1/6 of the interest coming due on the next succeeding interest payment date plus 1/12 of the next succeeding principal payment date shall be paid into a "Sinking Fund".

Note 6. Interest Cost

It is the Waterworks policy to capitalize interest cost on construction in progress to the extent such construction is capitalized on the statement of net assets. For the year ended June 30, 2006 the Waterworks incurred total interest cost of \$50,248 and no interest costs were capitalized.

Note 7. Pension and Retirement Benefits

The Waterworks contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 3.70% of their annual salary and the Waterworks is required to contribute 5.75% of annual covered payroll. Contribution requirements are established by state statute. The Waterworks contributions to IPERS for the years ended June 30, 2006, 2005, and 2004 were \$14,436, \$14,984 and \$17,700 respectively, equal to the required contributions for each year.

Note 8. Risk Management

The Chariton Municipal Waterworks is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Waterworks assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 9. Commitments/Subsequent Event

The Waterworks has entered into written contracts for various construction projects. At June 30, 2006, the uncompleted contract amounts totaled approximately \$500,000. These amounts will be paid as work on the projects progresses. It is anticipated these projects will be completed in fiscal year 2007.

The Waterworks was awarded an \$800,000 State Revolving Fund loan from the Iowa Department of Natural Resources. As of June 30, 2006, no loan monies were received by the Waterworks. However, the Waterworks will receive this loan money in fiscal year 2007 in order to fund large construction projects.

Required Supplementary Information

CHARITON MUNICIPAL WATERWORKS

BUDGETARY COMPARISON SCHEDULE
OF RECEIPTS, DISBURSEMENTS AND CHANGES IN BALANCES -
BUDGET AND ACTUAL (CASH BASIS)

REQUIRED SUPPLEMENTARY INFORMATION

Year ended June 30, 2006

	Proprietary Funds Actual	Budgeted Amounts		Final to Actual Variance
		Original	Final	
Receipts:				
Use of money and property	\$ 29,042	4,000	4,000	25,042
Charges for service	1,101,517	1,024,350	1,024,350	77,167
Miscellaneous	35,718	22,200	22,200	13,518
Total receipts	1,166,277	1,050,550	1,050,550	115,727
Disbursements:				
Business type activities	1,266,791	1,050,550	1,125,550	(141,241)
Total disbursements	1,266,791	1,050,550	1,125,550	(141,241)
Excess (deficiency) of receipts over over (under) disbursements	(100,514)	-	(75,000)	(25,514)
Other financing sources, net	-	-	-	-
Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses	(100,514)	-	(75,000)	(25,514)
Balances beginning of year	800,546	-	-	800,546
Balances end of year	\$ 700,032	-	(75,000)	775,032

See accompanying independent auditor's report.

CHARITON MUNICIPAL WATERWORKS
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION

Year ended June 30, 2006

	Proprietary Funds		
	Cash Basis	Accrual Adjustments	Accrual Basis
Revenues	\$ 1,166,277	6,508	1,172,785
Expenses	1,266,791	(199,274)	1,067,517
Net	(100,514)	205,782	105,268
Other financing sources, net	-	-	-
Beginning net assets	800,546	2,671,514	3,472,060
Ending net assets	\$ 700,032	2,877,296	3,577,328

See accompanying independent auditor's report.

CHARITON MUNICIPAL WATERWORKS

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING

Year ended June 30, 2006

The Chariton Municipal Waterworks prepares a budget on the cash basis of accounting and submits it to the City Council. In accordance with the Code of Iowa, the City Council annually adopts a budget on the cash basis following required public notice and hearing for all funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized on the cash basis budget and appropriations lapse at year end. The budget approved by the City Council includes the budget of the Waterworks.

Formal and legal budgetary control is based upon classes of disbursements, known as functions, not by fund. The Waterworks disbursements are budgeted in the business type activities function. During the year, one budget amendment increased budgeted disbursements by \$75,000. The budget amendment is reflected in the final budgeted amounts.

During the fiscal year ended June 30, 2006, Waterworks disbursements exceeded the amounts budgeted.

Other Supplementary Information

CHARITON MUNICIPAL WATERWORKS

Schedule 1

SCHEDULE OF OPERATING EXPENSES

Year ended June 30, 2006

Plant Operation	
Salaries	\$ 113,782
Power and propane	47,563
Chemicals	100,825
Supplies	6,188
Telephone	807
Maintenance materials and labor	3,085
Other expenses	2,438
Total plant operation	<u>\$ 274,688</u>
Distribution Operation	
Salaries	\$ 70,979
Vehicle maintenance	9,377
Insurance	36,109
Supplies	6,177
Utilities	2,633
Telephone	2,026
Maintenance material and labor	63,719
Other expenses	1,023
Total distribution operation	<u>\$ 192,043</u>
Accounting and Collection	
Salaries	\$ 79,908
Meter reading	8,013
Office supplies	3,986
Sales tax	53,611
Postage	9,464
Telephone	2,477
Utilities	4,778
Other expenses	2,135
Total accounting and collection	<u>\$ 164,372</u>
Administration	
Employee benefits	\$ 75,978
Audit and filing fee	2,340
Safety, schools, miscellaneous	24,039
Building expense	2,806
Engineering	7,500
Total administration	<u>\$ 112,663</u>
Repairs and Minor Equipment	
Plant improvements	\$ 3,691
Office equipment	2,020
Distribution improvements	10,423
Total repairs and minor equipment	<u>\$ 16,134</u>
Depreciation and Amortization	
Depreciation	\$ 254,531
Amortization	2,838
Total depreciation and amortization	<u>\$ 257,369</u>

See accompanying independent auditor's report.

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Independent Auditor's Report on Internal Control
over Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in Accordance
with Government Auditing Standards

To the Board of Trustees
Chariton Municipal Waterworks

We have audited the accompanying financial statements of the business type activities of the Chariton Municipal Waterworks, Chariton, Iowa, as of and for the year ended June 30, 2006, which collectively comprise the Waterworks basic financial statements listed in the table of contents and have issued our report thereon dated September 26, 2006. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Chariton Municipal Waterworks internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Chariton Municipal Waterworks ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in Part I of the accompanying Schedule of Findings.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we believe they are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Chariton Municipal Waterworks financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non-compliance that are described in Part II of the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the Waterworks operations for the year ended June 30, 2006 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Waterworks. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

This report, a public record by law, is intended for the information and use of the officials, employees and citizens of the Chariton Municipal Waterworks and other parties to whom the Chariton Municipal Waterworks may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Chariton Municipal Waterworks during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Peak & Gerdes, LLP
Certified Public Accountants

September 26, 2006

CHARITON MUNICIPAL WATERWORKS

SCHEDULE OF FINDINGS

Year ended June 30, 2006

Part I: Findings Related to the Financial Statements

INSTANCES OF NONCOMPLIANCE

No matters were reported.

REPORTABLE CONDITIONS

- I-A-06 Segregation of Duties – One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The issuance of receipt slips, bank deposits and the posting of the cash receipts to the accounting records are sometimes all done by the same person.

Recommendation – We realize that with a limited number of office employees, segregation of duties is difficult. However, the Waterworks should review its control procedures to obtain the maximum internal control possible under the circumstances.

Response – We will consider this.

Conclusion – Response acknowledged. The Waterworks could segregate duties to the extent possible with existing personnel and utilize administrative personnel to provide additional control through review of financial transactions and reports.

- I-B-06 Transaction Recording – We noted that funds in a money market account at one bank were transferred to a certificate of deposit at another bank; however, this transaction did not go through the receiving bank account. The disbursing bank issued a cashier's check to the Waterworks, and the Waterworks then endorsed the cashier's check and gave it to the receiving bank in order to purchase a certificate of deposit.

Recommendation – In the future, all transfers between banks should be deposited to a bank account, with the related disbursement coming out of the bank account. Also, the use of cashier's checks should be eliminated.

Response – We will implement this recommendation.

Conclusion – Response accepted.

CHARITON MUNICIPAL WATERWORKS

SCHEDULE OF FINDINGS

Year ended June 30, 2006

Part II: Other Findings Related to Statutory Reporting

II-A-06 Certified Budget - The budget certified by the City of Chariton includes amounts budgeted for the Chariton Municipal Waterworks. Disbursements during the year ended June 30, 2006, exceeded the amounts budgeted in the business type activities function of the Chariton Municipal Waterworks.

Recommendation – The budget should have been amended and submitted to the City Council for approval before disbursements were allowed to exceed the budget.

Response – The budget will be amended in the future, if applicable.

Conclusion – Response accepted.

II-B-06 Questionable Disbursements - We noted no disbursements that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

II-C-06 Travel Expense - No disbursements of Waterworks money for travel expenses of spouses of Waterworks officials or employees were noted.

II-D-06 Business Transactions - No business transactions between the Waterworks and Waterworks officials or employees were noted.

II-E-06 Bond Coverage - Surety bond coverage of Waterworks officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

II-F-06 Board of Trustee Minutes - No transactions were found that we believe should have been approved in the trustee minutes but were not.

II-G-06 Deposits and Investments - The Waterworks investment policy refers to an outdated section of the Code of Iowa.

Recommendation – The Waterworks investment policy which currently refers to Chapter 453 of the Code of Iowa, should be amended to the current chapters of 12B and 12C of the Code of Iowa, which cover governmental investment guidelines.

Response – We will amend our investment policy.

Conclusion – Response accepted.

II-H-06 Revenue Bonds - The Waterworks has complied with the provisions of the revenue bond indentures.

CHARITON MUNICIPAL WATERWORKS

SCHEDULE OF FINDINGS

Year ended June 30, 2006

II-I-06 Revenue Bonds Interest - The average interest rate on the remaining portion of the 1992 bond issue is in excess of 6%. The bond agreements allow the Waterworks to refinance or pay off these bonds. The Waterworks currently has the funds available to pay off these bonds. If the Waterworks paid off these bonds, a significant amount of interest could be saved.

Recommendation - The Waterworks analyze all aspects of its operation, including financing decisions, to ensure the business decisions made are prudent and efficient.

Response - We will continually review the financing decisions to ensure the decisions made are prudent and efficient.

Conclusion - Response accepted.

II-J-06 Delinquent Accounts - For delinquent water service accounts, the Waterworks does not turn over the accounts to the County Treasurer for collection.

Recommendation - The Waterworks consider turning over the delinquent accounts to the County Treasurer for collection.

Response - We will review this issue.

Conclusion - Response accepted.

II-K-06 Payroll - We noted that there was not always written authorization for employee pay rates.

Recommendation - Written authorization of pay rates should be obtained for all employees.

Response - We will attempt to implement this recommendation.

Conclusion - Response accepted.

II-L-06 Meter Reader - The contract with the Waterworks meter reader does not document the minimum vehicle and general liability insurance required.

Recommendation - The Waterworks require that the contract with the meter reader include the minimum vehicle and general liability insurance required for the position.

Response - We will implement this recommendation.

Conclusion - Response accepted.

CHARITON MUNICIPAL WATERWORKS

SCHEDULE OF FINDINGS

Year ended June 30, 2006

II-M-06 Electronic Check Retention – Chapter 554D.114 of the Code of Iowa allows the Waterworks to retain cancelled checks in an electronic format and requires retention in this manner to include an image of both the front and the back of each cancelled check. The Waterworks retains cancelled checks through electronic image, but does not obtain an image of the back of each cancelled check as required, for some bank accounts.

Recommendation – The Waterworks should obtain and retain an image of both the front and back of each cancelled check as required.

Response – We will implement this recommendation.

Conclusion - Response accepted.

II-N-06 Telephone – The Waterworks provides Waterworks-owned cellular phones to certain employees for Waterworks business. However, the Waterworks does not have a specific policy addressing the use of Waterworks-owned cellular phones.

Recommendation – The Waterworks should establish a policy to address the use of Waterworks-owned cellular phones, including restricting use by employees of the Waterworks to Waterworks related business.

Response – We will review this and take action as necessary.

Conclusion- Response accepted.

II-O-06 Compliance Issues – Chapters 384.95 to 384.103 of the Code of Iowa requires that for public improvements which cost in excess of \$25,000, an advertisement for sealed bids and a public hearing be held in the time frame as provided in Chapter 362.3 of the Code of Iowa. In some cases, it appears that these requirements were not met for the various construction projects.

Recommendation – For public improvement projects which cost in excess of \$25,000, the Waterworks implement procedures to ensure the requirements as noted per the Iowa Code are met.

Response – We will implement this recommendation.

Conclusion – Response accepted.